LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 7088 **NOTE PREPARED:** Jan 12, 2013
BILL NUMBER: HB 1553 **BILL AMENDED:**

SUBJECT: Tax Incentives for New Employees.

FIRST AUTHOR: Rep. Moed **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: X **GENERAL** **IMPACT:** State
DEDICATED
FEDERAL

Summary of Legislation: This bill creates the Hoosier Job Creation Tax Credit (HJC). The credit is provided to small businesses who hire a sufficient number of qualifying new employees after December 31, 2012, and before January 1, 2016. The bill defines a qualifying employee as a person who meets one of the following conditions:

- Receiving unemployment benefits or have exhausted their unemployment benefits.
- Are former members of the armed services of the United States or the National Guard.

Effective Date: January 1, 2013 (retroactive).

Explanation of State Expenditures: *Department of State Revenue (DOR):* The DOR will incur additional expenses to revise forms, update instructions, and modify the existing tax processing system to implement this bill. The DOR's current level of funding and resources should be sufficient to administer this tax credit.

Indiana Department of Workforce Development (DWD): The bill requires the DWD to provide the essential employer payroll information to the DOR to administer the tax credit. The DWD's current level of resources should be sufficient to comply with the provisions of the bill.

Explanation of State Revenues: *Summary* - The credit would be effective for small businesses that hire and retain qualified new employees in tax years 2013, 2014, and 2015. The tax credit could potentially reduce state General Fund revenue by an estimated \$44.3 M and \$61.7 M per year from FY 2014 to FY 2016 for small businesses in existence in the first quarter of 2012. This estimate is based on a simulation using 2011 and 2012 quarterly census of employment and wages data. The potential revenue loss from small businesses that began operations sometime during the last three quarters of 2012 is indeterminable, but assumed to be significant.

The credit can be used to offset tax liabilities from the Individual Adjusted Gross Income Tax, Corporate Adjusted Gross Income Tax, Financial Institutions Tax, and Insurance Premiums Tax. Revenue collected from those taxes are deposited in the General Fund. The credit is nonrefundable, but unused credits may be carried forward for up to three years. Unused credits may not be carried back. The fiscal impact of this tax credit would likely occur in FY 2014, FY 2015, and FY 2016, but the fiscal impact could begin in FY 2013 if taxpayers that hire qualified new employees in the first half of 2013 change their quarterly estimated payments.

Background Information: The tax credit is $3,000 per qualified new employee employed during the tax year, up to a maximum of $100,000 per small business in a tax year. The tax credit is limited to taxpayers that:

- Began operations with full-time employees in Indiana before January 1, 2013.
- Employ no more than 150 employees on at least 50% of the business working days.
- Have a majority of their employees working in Indiana.

A small business is entitled to the credit for the qualified new employees it employs during 2013, 2014, or 2015 in excess of its base employment level. The base employment level is: (1) the average employment by the small business during the first six months of 2011, if the small business was in existence and operating in Indiana on January 1, 2011; or (2) the average employment by the small business during its initial six months of operation, if the small business began doing business in Indiana after January 1, 2011 but before January 1, 2013. The bill also contains a clawback provision under which the small business would forfeit 50% of the tax credit if the qualified new employee is not retained for at least 18 months after initial employment.

A qualified new employee must be employed for at least 35 hours per week and be paid an income of at least 200% of the federal hourly minimum wage. In addition, the qualified new employee must meet all of the following criteria:

- Initially hired as a full-time employee for the first time after December 31, 2012.
- Is receiving or has exhausted state or federal unemployment benefits at the time of the initial hire or is a former member of the U.S. military who served on active duty and received an honorable discharge.
- Is not employed by a related member or business entity of the small business within a year of the initial hire by the qualifying business.
- Is not a child, grandchild, parent, or spouse of any individual who is an employee of the small business or who has a direct or an indirect ownership interest of at least 5% of the business.

The revenue loss estimates are based on a simulation performed using an extract of quarterly census of employment and wages reports filed for purposes of unemployment compensation taxes. The extract is comprised of firms that had employees in January 2012 and each firm's reported wages and number of employees from 2011 and the first quarter of 2012. Each firm was evaluated using the criteria for a qualifying employer. Then, the base period employment was derived for all qualifying employers, and the tax credit for each qualified firm was computed using the rules within the bill. This analysis yielded 102,695 small business firms. Of those firms, 44,355 had an average employee wage above the qualifying threshold of $30,305 as of the first quarter 2012.

The bill stipulates that the credit can only be awarded if the new employee has received unemployment benefits

or is a veteran. Using information from the Bureau of Labor Statistics, the probability a new hire was laid-off and received unemployment benefits was computed to be 41.3%. This statistic was derived from the Job Openings and Labor Turnover data from 2011. Meanwhile the U.S. Department of Labor reports that veterans comprise 7% of the national workforce. Applying those two statistics and adjusting for the interaction, the total revenue loss for only qualifying employees is estimated to be approximately $42.6 M.
The lower and upper range of the estimated revenue loss is based on the estimated response of new hiring to the reduction in the wage cost from the tax credit. The response effect was derived from research conducted on the percentage change in employment given a 1% change in wages. The tax credit reduces a firm's average labor cost. The response rates are assumed to range from a 1% to 5% increase in employment for a 10% reduction in wage cost.

The credit is nonrefundable, so a business can only claim a credit amount to reduce their tax liability to zero. This attribute of the tax credit will likely reduce overall revenue loss and spread out the credits across the carryover period of 3 years.

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue; Indiana Department of Workforce Development.

Local Agencies Affected:

Information Sources: LSA Unemployment Payroll Reporting Database; Bureau of Labor Statistics, *Job Openings and Labor Turnover Reports,* 2002-2012; U.S. Department of Labor, *The Veteran Labor Force in the Recovery,* November 2011; Sasser, Alicia, *New England Public Policy Center: The Potential Economic Impact of Increasing the Minimum Wage in Massachusetts*, January 2006.

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